ConsumersUnion
POLICY & ACTION FROM CONSUMER REPORTS

January 20, 2012

Via email to MLRadjustments@HHS.gov
The Honorable Kathleen Sebelius
Department of Health and Human Services
200 Independence Avenue, S.W.
Washington, DC 20201

Dear Secretary Sebelius:

Consumers Union, the policy and advocacy division of *Consumer Reports*, submits these comments regarding North Carolina's request for an adjustment to the medical loss ratio (MLR) requirement, submitted by the North Carolina Department of Insurance (NCDOI). We urge the Department of Health and Human Services (HHS) to give all North Carolina consumers the immediate full benefit of the MLR rule by denying NCDOI's request to phase in the rule at 72% in 2011, 74% in 2012, and 76% in 2013.

If NCDOI's application is granted, consumers could lose up to $18.3 million in rebates for the years 2011-2013, based on 2010 loss ratio data. NCDOI must show that applying the 80% standard is reasonably likely to "destabilize" the state's individual market.

We share NCDOI's concern that North Carolina's individual market is concentrated, but NCDOI has not shown that applying the 80% minimum beginning in 2011 is reasonably likely to result in fewer choices for consumers. To the contrary, the evidence shows that carriers covering about 84% of the individual market already met the standard in 2010. Those that did not meet the standard in 2010 have adjusted pricing to meet it in 2011, or they are financially able to pay rebates if required.

NCDOI's application rests heavily on the comments of the state's second largest individual market carrier, Wellpath Select, Inc., which had an adjusted MLR of 69.9% in 2010. Wellpath claims that it needs more time to adjust its business model; however, as described further below, Wellpath would remain profitable if in fact it must pay rebates on an 80% basis beginning in 2011. In addition, the data indicates that Wellpath's and other carriers' changes to broker compensation are unlikely to harm consumers' ability to find assistance in buying coverage.

In the absence of evidence of a likelihood of destabilization, consumers who are struggling to afford health insurance should not be denied the full benefit of the MLR rule.

The Data Does Not Show That A Destabilizing Number Of Issuers Are Reasonably Likely To Exit The State

A. **Carriers covering the vast majority of consumers already meet the standard, or are adjusting business models to meet it in 2011**.

NCDOI's application shows that carriers covering more than 85% of consumers in the individual market already met the 80% MLR standard in 2010, or have adjusted pricing to meet it in 2011. We share NCDOI's concern that North Carolina's individual market is concentrated, with 81% of consumers in Blue Cross and Blue Shield plans. But NCDOI's application shows that several big-name competitors will remain in the market even if an adjustment is not granted, including Aetna Life Insurance Co, Wellpath Select (Coventry Health Care), Golden Rule Insurance Co. (United Health Group), and Humana Insurance Co.

In fact, at least nine carriers subject to the MLR rule will continue to serve the individual market. Nine additional smaller carriers, not subject to the rule, also provide coverage in the individual market.[1] None of these 18 carriers have stated that they intend to exit.

Further, of the nine active carriers subject to the rule, Blue Cross Blue Shield of North Carolina and Aetna already meet the 80% standard, while three others – Celtic Insurance Co., Humana, and National Foundation Life Insurance Co. – have begun pricing to meet the standard in 2011. All three stated that they do not need additional time to fully comply.

The remaining four carriers, covering about 10% of the individual market, did not meet the 80% standard in 2010 and have expressed a need for additional time to adjust their business models. But a close look at these companies shows that they should not need to delay implementation of the MLR rule:

- Wellpath Select, Golden Rule and John Alden Life Insurance Co. would all remain profitable on an after-tax consolidated basis after paying estimated rebates based on an 80% standard. **See Table 1**.
- Golden Rule and John Alden would be profitable on an after-tax individual market basis.
- Time Insurance Co. and John Alden are part of Assurant. HHS already has found, based on the statements of Assurant, that the company "has been able to successfully streamline its expense structure during 2011," mitigating concerns that the company would not be able to reduce expenses to remain profitable in 2011.[2]
- Wellpath is owned by Coventry Health Care, which has already started accounting for estimated 2011 rebates in its 2011 consolidated financial statements. Coventry reported net

[1] NCDOI's application does not indicate whether all of the smaller non-credible carriers are actively marketing policies.
[2] *See* Department of Health and Human Services, Letter to Commissioner Stephen W. Robertson, November 27, 2011, at pg. 8.

earnings of about $123 million in the 3rd quarter, and $457 million in the first nine months of 2011 after estimated rebates.[3]

- None of the four carriers have stated that they will exit the market if the adjustment is not granted.
- The estimates of post-rebate profits do not account for any changes the carriers have made in 2011 to meet or come closer to the 80% target.

Table 1: Profitability of Active Carriers Below 80% Seeking More Time to Adjust Business Models, Based on 2010 Financials

	2010 PPACA MLR	**Estimated rebates at 80%**	**After-tax consolidated profit after paying estimated 80% rebates**
Golden Rule Ins. Co.	64.7%	$3,102,105	$382,929
John Alden Life Ins. Co.	52.3%	$945,877	$465,109
Wellpath Select, Inc.	69.9%	$3,739,634	$5,490,792
Time Ins. Co.	67.5%	$2,650,265	$(1,041,903)[4]

B. Smaller carriers that have ceased marketing policies did not do so as a direct result of the MLR rule and have not destabilized the market.

As evidence of potential market destabilization due to the MLR rule, NCDOI reports that two carriers, American Republic Insurance Co. and World Insurance Co., have exited the individual market, and five carriers have "ceased marketing policies." These five carriers apparently will continue to service their current customers but will not market new coverage. The five carriers are MEGA Life and Health Insurance Co., Mid-West National Life Insurance Co. of Tennessee, American Medical Security Life Insurance Co., American National Life Insurance Co. of Texas and Standard Life and Accident Insurance Co. Combined, the seven carriers represent a very small portion of the individual market – just 3.1%.

As noted in a prior HHS decision, the two exiting carriers, American Republic and World, are part of the American Enterprise Group, which is withdrawing in all states in which it conducts individual market business, and its decision to do so appears to be unrelated to the risk of paying rebates.[5] In addition, both companies met the 80% standard in 2010 and are not

---

[3] *See* Coventry Health Care Inc., Third Quarter 10-Q, Consolidated Statements of Operations, filed on November 4, 2011. Coventry stated that it has a "detailed projection process" to estimate MLR rebates, and has recorded them as Accounts Payable and Other Accrued Liabilities in its balance sheets and as "contra-revenue" in its Managed Care Premium line of financial statements. See page 6.

[4] While Time projects losses based on 2010 data, as noted above, Time's parent company has reported that it has successfully streamlined its expense structure to remain profitable.

[5] *See* Department of Health and Human Services, Letter to Commissioner Stephen W. Robertson, November 27, 2011, at pg. 6.

projected to owe rebates for 2011. Celtic Insurance Co. has agreed to offer their 2,406 customers guaranteed-issue replacement coverage.

The parent company of both MEGA and Mid-West, HealthMarkets, Inc., decided *in early 2010* to "significantly reduce the number of states in which the Company would market its health benefit plans in the future." HealthMarkets gave three reasons for the change: (1) health reform legislation, including MLR requirements and elimination of most annual benefit caps; (2) a decision to refocus the business on the company's Insphere insurance sales agency, launched in 2009 to sell supplemental insurance products and health insurance from unaffiliated third-party companies; and (3) in states where Insphere distributes third-party plans, those plans have largely outsold the company's own offerings.[6] HealthMarket's broader change in strategy means that MEGA and Mid-West would have ceased selling in North Carolina regardless of whether the state obtains an adjustment.

NCDOI reported that American Medical Security, with 1,331 members in North Carolina, stopped marketing new policies in May 2010. American Medical sells association and individual plans and is a subsidiary of Golden Rule and part of the United Health Group. NCDOI has not indicated why American Medical stopped selling in North Carolina, but based on 2010 data, the company was already meeting the MLR standard. Thus, its decision was not due to an inability to meet the MLR rule.

Finally, NCDOI states that American National Life of Texas and Standard Life and Accident "indicated that they would seriously consider re-entering the market if North Carolina was granted an adjustment to the 80% MLR requirement." But it is not clear why NCDOI states that they would re-enter if an adjustment would be granted, as these carriers, both part of American National Insurance Co., were too small to be subject to the MLR rule. Therefore, their decision to cease selling was not likely to be based on the new standard, and their decision to re-enter the market should not be affected by a delay in the MLR rule.

Some business restructuring must occur in the wake of the Affordable Care Act if consumers are to realize the benefits of the Act's insurance market reforms. While some of the smaller carriers operating in North Carolina have stopped selling individual market coverage as part of broader strategy changes, NCDOI has not demonstrated that their decisions were due primarily to the MLR rule, or that they have caused market destabilization.

The Number Of Enrollees Potentially Affected Represents A Small Slice Of The Market

The nine active carriers subject to the rule have not indicated that they will exit the market absent an adjustment. Therefore, we would not expect any consumers to be impacted if HHS denies the adjustment. The insurers who reportedly have ceased marketing new policies covered just 3.1% of the market, or 12,977 residents. Most of these enrollees will continue to

[6] HealthMarkets, Inc., Form 10-K filing with the U.S. Securities and Exchange Commission, March 16, 2011.

be covered by their current insurer, and those with American Republic or World will be offered Celtic plans.

Even under a highly unlikely worse-case scenario, in which, for example, the carriers who stated that they want more time to adjust exited the market, the number of enrollees impacted would be about 41,961 enrollees out of 416,357 total, or 10% of the market. If Time, the one insurer that would not be profitable in North Carolina after rebates based on 2010 data, exited the market, the number of enrollees affected would be 9,788, or 2.35% of the market. Again, however, we emphasize that Time is unlikely to withdraw, as its parent company has already stated that it is adjusting business models to meet the MLR standard and remain profitable.

There Is Scant Evidence That Changes To Broker Compensation Will Result In Reduced Access To Agents And Brokers

According to NCDOI, at least four North Carolina carriers reported that they have already cut commissions and several said that they have "lock-in" contracts preventing them from changing commission rates on renewal business, making it harder to meet the 80% rule.

Wellpath Select, in particular, argues that its commission changes "have created significant disruption to the market and to consumer access to our individual product, which is reflected in a material decrease in policies issued to new members." Wellpath states that policies issued to members decreased by 11% from January to October 2011 compared to the same period in 2010. The company also states that the number of brokers selling its products dropped by 62% from January to September 2011.

Wellpath attributes the drop in brokers selling its products to the company's decision to cut its typical commission structure from 27%/7% for first year/renewals to 14%/4%. However, Wellpath's new commission structure continues to be highly competitive when compared to individual market structures paid in other states.[7] In addition, as Table 2 shows, Wellpath far exceeded both the nationwide and statewide average individual market agent/broker compensation paid as a percent of premium and on a per member per month basis.[8]

---

[7] *See* National Association of Health Underwriters, Blinded Survey of Broker Compensation Data, 2009-2011.
[8] Data in the table is based on the 2010 SHCE filings and on national averages provided in the NAIC, Report of the Health Care Reform Actuarial (B) Working Group to the Health Insurance and Managed Care (B) Committee on Referral from the Professional Health Insurance Advisors (EX) Task Force Regarding Producer Compensation in the PPACA Medical Loss Ratio Calculation, May 26, 2011.

Table 2: Comparison of Individual Market Agent/Broker Fees and Commissions, Calculated from 2010 Data*

Agent/Broker Fees and Commissions As Percent of Premium		Agent/Broker Fees and Commissions Paid Per Member Per Month	
National Foundation	25.3%	National Foundation	$33.60
Wellpath Select	12.3%	Wellpath Select	$21.27
Golden Rule	10.2%	Time	$18.15
Time	9.9%	Golden Rule	$16.90
Mid-West Nat'l of TN	8.9%	Mid-West Nat'l of TN	$15.33
Celtic	7.9%	John Alden	$13.45
John Alden	6.3%	Celtic	$12.40
American Medical	5.5%	American Medical	$11.98
BCBS NC	4.6%	BCBS NC	$9.62
MEGA	2.9%	MEGA	$7.48
Humana	2.6%	Aetna	$3.47
Aetna	2%	Humana	$3.46
Average	**5.2%**	**Average**	**$10.63**
National Average	**5.86%**	**National Average**	**$12.28**

*Excludes exiting carriers, American Republic and World. Figures are rounded.

Consumer access to brokers and agents is important, so long as consumer receive *unbiased* sales information. Sales that may be the result of higher-than-market commissions may not be in the best interest of consumers. By creating a more level playing field with respect to broker commissions, the MLR rule may prevent steering and foster competition based on value, not on how much brokers are paid. The evidence of commission cuts is outweighed by the benefits to consumers of the rule's incentives for increased carrier efficiency, including fairer broker and agent compensation.

We also note that, to its credit, the NCDOI has used federal grant funds to launch and promote a new program, Smart NC, which promises to help consumers "identify enrollment opportunities for health insurance coverage."[9] Consumers have options beyond brokers and agents when they are searching for guidance in buying coverage.

[9] See http://www.ncdoi.com/Smart/.

Additional Factors Do Not Weigh In Favor Of Granting An Adjustment

NCDOI asserts that the MLR rule creates a "barrier to entry and a barrier to growth" because it does not account for generally lower loss ratios in the early years of a policy and increases throughout the life of the policy. However, NCDOI's concern is unfounded. The MLR rule provides flexibility to allow entry and growth for new carriers.[10]

NCDOI also expresses a concern that "in an effort to meet the 80% MLR requirement, issuers will cease marketing the lower-cost leaner plans in favor of higher-cost plans with lower cost sharing" because higher cost plans provide a higher premium base over which to spread administrative costs. NCDOI offers no specific evidence to support its concern. Wellpath Select cites one example of a lower cost high deductible plan (19A) that "will likely be removed" from the market absent an adjustment because Wellpath "simply will be unable to offer a product on a continued basis that provides less than $20 per member per month for total administrative services, including commissions, and does not cover its costs."[11]

NCDOI's and Wellpath's statements fail to show that an adverse impact on market premiums is likely. First, NCDOI's application does not provide comprehensive information about the products and premiums available, making it impossible to assess the validity of these concerns and the potential impact on the market.

In addition, the MLR rule includes provisions that address Wellpath's concerns. The rule allows carriers to aggregate all products in the market segment when calculating the ratio. A company with sufficient enrollment and breadth of plan choices, including both high and low deductible plans, would be able achieve a balance of plans with lower expense margins against those with higher expense margins when calculating the MLR. Small to mid-size carriers, such as Wellpath, are able to apply a credibility adjustment which allows them to increase the MLR by a deductible factor that is based on the average deductible of all policies included in the MLR calculation.

Moreover, Wellpath offers little explanation as to how a transition period would allow it to solve its purported inability to offer lower premium products with the 80% MLR standard.

The MLR rule gives insurers ample room to turn a profit while providing an incentive for them to keep unnecessary costs down. NCDOI's application does not show an impact on premiums, benefits, and cost-sharing that is likely to destabilize the market.

---

[10] The rule allows carriers to defer experience of new policies when more than half of premium revenue is derived from newly issued policies. *See* Code of Federal Regulations, Title 45, Section 158.121. The rule also allows carriers to count payments into contract reserves created early in the life of a policy as claims, so long as they subtract later withdrawals from those reserves from claims. *See* Code of Federal Regulations, Title 45, Section 158.140.

[11] It is not clear whether Wellpath has accounted for its credibility adjustment and other PPACA adjustments that go into the MLR calculation when it determined that it cannot offer a product that provides less than $20 per member for administrative services.

Conclusion: NCDOI Has Not Demonstrated A Reasonable Likelihood Of Destabilization And North Carolina's Individual Insurance Market Is Well-Positioned To Adjust To The MLR Requirement

With more than 85% of members already in plans that already meet the new MLR standard or have adjusted pricing to do so, North Carolina is very close to achieving better value for *all* of its individual market consumers. And although the new rule is designed to improve efficiency and value for consumers, carriers who are projected to have an MLR below the new 80% standard have adequate profit margins to refund consumers if needed.

NCDOI's application does not demonstrate a likelihood of destabilization of the individual market. HHS should reject the request and require all North Carolina individual market carriers to improve value for consumers struggling with rising premiums.

Sincerely,

Sondra Roberto
Staff Attorney
Consumers Union